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JAPAN · ECONOMIC · INSTITUTE

JEI REPORT

A Two-Part Report: A and B

NO. 43B
November 15, 1991

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Cancellation Of Bush's Asian Trip Stirs Washington, Tokyo Reactions

When the White House announced November 5 that President Bush's late November trip to Japan and other Asian countries had been canceled, the chief executive may have created more public relations problems than he had hoped to solve by curtailing his foreign travel. In the domestic arena some political commentators and members of the president's own party criticized the decision as a precipitate response to Democratic charges that Mr. Bush focuses on foreign policy at the expense of domestic issues. Despite White House denials, cancellation of the Asian tour had a particular political cast because it was announced the evening of an election day in which some key Republicans were defeated in state and local races.

Prime Minister Kiichi Miyazawa tactfully said that he understood why Mr. Bush could not visit Japan as planned, but statements by other Japanese officials suggest disappointment in Tokyo. Mr. Miyazawa viewed the president's visit as an important opportunity to develop a joint declaration of a global partnership between the United States and Japan in the post-Cold War era. The cancellation of Mr. Bush's trip obviously delays issuance of this important

visit, Secretary of State Baker presented much of the message to Japan that the president presumably would have delivered. In a November 11 speech to the Tokyo-based Japan Institute for International Affairs Mr. Baker emphasized Washington's interest in the Asian Pacific region, saying, "America's fate is ever more closely tied to East Asia and the Pacific." In what was billed as the major speech of his week-long tour of the Asian region Mr. Baker also sought to assure his audience that, despite U.S. troop reductions in Japan and elsewhere in the region, the U.S. commitment to Japanese security remains "unshakable." In addition, the secretary of state used his address to nudge Japan toward greater assumption of global political responsibilities, urging Tokyo to go beyond "checkbook diplomacy," an apparent reference to Japan's provision primarily of money to support the coalition forces that fought in the Persian Gulf War.

Barbara Wanner

Japan's Balance Of Payments Surplus Rises Again

Japan's latest balance of payments statistics, released November 1, captured the gloominess of late autumn for those on either side of the Pacific who worry that the current account surplus, which fell by more than half between its 1987 peak and 1990, is again on the upswing. Compared to a year earlier, Japan's dollar-denominated current account surplus soared 161.5 percent in the July-September period (see Table 1). That represented the second straight quarter of a year-to-year surge after nine straight quarters of decline.

For Americans hoping for a smaller trade imbalance and struggling with a sluggish economic recovery, the news was not only depressing but surprising. One of the very few silver linings that a nation under a recessionary cloud can expect is either a smaller current account deficit or a larger surplus. Based on U.S. data through the second quarter the American current account deficit with Japan declined substantially over the past year. Although third-quarter data are not yet available on a bilateral basis, Japan's surging overall current account surplus for the period indicates that the U.S.-Japan imbalance probably has shown little additional movement despite weak import demand in the United States.

Japanese analysts have tended to interpret the latest balance of payments statistics as an inevitable reaction to unsustainable developments in 1990. This argument has two parts: one, as noted above, suggests that weak demand in the United States and other major export markets because of recession or slow growth last year reduced Japanese exports below the levels they otherwise would have reached. The other part is that Japan's imports in 1990 were abnormally high due to the now widely recognized financial "bubble;" that phenomenom led to inflated imports of luxury cars, paintings and other expensive goods. In short, this argument continues, no one should have expected Japan's balance of payments surplus in 1991 to have equaled 1990's level of $35.8 billion absent these special influences, which now have been reversed. This argument concludes with the observation that Japan's own economic growth rate in mid-1991 may have been below that of its trading partners, implying weak demand for imports and relatively buoyant export demand. This line of reasoning meshes neatly with recent estimates that Japan's current account surplus in 1991 is likely to exceed $60 billion, or approximately the 1989 level.

Table 1: Japan's Balance of Payments

(in millions of dollars)

	Trade Balance	Exports (f.o.b.)	Imports (f.o.b.)	Services (net)	Current Account Balance	Long-Term Capital (net)
1986	$92,827	$205,591	$112,764	$-4,932	$85,845	$-131,461
1987	96,386	224,605	128,219	-5,702	87,015	-136,532
1988	95,012	259,765	164,753	-11,263	79,631	-130,930
1989	76,917	269,570	192,653	-15,526	57,157	-89,246
1990	63,528	280,374	216,846	-22,292	35,761	-43,586
1989: I	21,311	66,945	45,634	-3,595	16,064	-5,612
II	19,794	66,560	46,766	-4,892	14,283	-30,801
III	19,770	68,157	48,387	-4,023	14,957	-21,559
IV	16,042	67,908	51,866	-3,016	11,853	-31,274
1990: I	14,393	65,460	51,067	-701	12,305	-16,086
II	13,614	65,510	51,896	-5,279	7,892	-18,985
III	17,149	70,500	53,351	-8,045	7,400	-7,247
IV	18,372	78,904	60,532	-8,267	8,164	-1,268
1991: I	20,729	74,978	54,249	-920	10,260	10,707
II	23,352	71,990	48,638	-4,064	18,664	-7,103
III(p)	33,836	76,931	43,095	-7,074	19,349	-9,885

These factors appear to have gone unforeseen by the Economic Planning Agency last December when it developed its FY 1991 economic outlook. EPA projected a current account balance of only $30 billion for the fiscal year ending March 31, 1992. This figure would have been a drop from $33.7 billion in FY 1990. In the first half of FY 1991 alone the current account surplus exceeded $38 billion, putting EPA's original estimate in the impossible dream category.

Normally, a surging Japanese current account surplus at least brings with it the benefit in American eyes of a larger outbound capital flow. However, the latest figures appear to offer confirmation of just the reverse: net Japanese foreign investment in securities has dropped sharply since the late 1980s (see Table 2). Furthermore, capital flows into Japan from the United States and Europe have jumped dramatically. In September foreigners pumped a net $9.1 billion into the Japanese stock market, the largest monthly amount ever. Largely as a result of these and other securities transactions, long-term capital showed an unusually sharp net inflow in the July-September quarter (Table 1). Offsetting this inflow and the larger current account surplus were substantial reductions in the net overseas short-term liabilities of Japanese foreign exchange banks. Such activity arguably helps drive down foreign interest rates, while it avoids stoking resentment toward rising Japanese foreign investment.

Most experts expect Japan's annual current account surplus to stabilize around $60 billion. For example, the International Monetary Fund, which predicts that the current account surplus will reach $62.7 billion in 1991,

Table 2: Japan's Net International Long-Term Securities Transactions

(in millions of dollars)

	Net Japanese Purchases			Net Foreign Purchases			Net
	Bonds	Stocks	Other*	Bonds	Stocks	Other**	Outflow
1986	$-93,024	$-7,048	$-1,905	$-2,109	$-15,758	$18,412	$-101,432
1987	-72,885	-16,874	2,002	6,675	-42,835	30,079	-93,838
1988	-85,812	-2,993	1,856	-21,628	6,810	35,116	-66,651
1989	-94,083	-17,887	-1,208	2,400	6,998	75,746	-28,034
1990	-28,961	-6,256	-4,464	16,991	-13,276	30,938	-5,028
1989: I	-14,003	104	577	-1,646	9,004	16,212	10,248
II	-25,091	-6,108	-776	-587	-6,196	27,501	-11,257
III	-25,871	-4,795	722	5,403	757	14,123	-9,661
IV	-29,118	-7,088	-1,731	-770	3,433	17,910	-17,364
1990: I	-869	-4,946	717	6,182	-11,713	8,246	-2,383
II	-9,353	-2,153	-954	4,975	838	723	-5,924
III	-10,905	-459	-2,405	4,790	-3,380	10,485	-1,874
IV	-7,834	1,302	-1,822	1,044	979	11,484	5,153
1991: I	-13,356	463	-1,348	1,418	17,486	9,129	13,792
II	-22,423	-2,840	-1,353	6,348	4,140	11,778	-4,350
III(p)	-11,120	-134	-94	9,509	15,245	13,317	26,723

*Yen-denominated bonds issued in Japan.
**Bonds issued outside of Japan by Japanese institutions.

Note: For outflows a minus sign indicates an increase in assets abroad. For inflows a positive value indicates an increase in Japanese liabilities to foreigners.

forecasts that the imbalance will fall slightly to $59.4 billion in 1992. These projections, of course, make assumptions about budget policy and investment intentions in Japan, the United States and elsewhere. Should Japan's economic malaise be deemed serious enough to warrant fiscal stimulation larger than now anticipated, increased demand on domestic capital markets would increase the yen's value, depress exports and lead to a smaller current account surplus.

Douglas Ostrom

Interest Rate Deregulation Hits Bumps

After several years in which Tokyo's plan to deregulate and reform domestic financial markets made significant strides, a major stumbling block has arisen for one of the most important parts of the plan -- replacing the rigid structure of government-determined interest rates paid on deposits with a system of market-determined ones. Interest rate deregulation has proceeded to the stage at which midsized and small financial institutions are being forced to undergo the inherently painful process of restructuring. Liberalization of interest rates will not be finished, however, without a definition of the role of